A.K. Capital Finance Limited

July 27, 2021

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Non-Convertible Debentures	100.00 (Rs. Hundred crore only)	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Assigned

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating assigned to proposed Non-Convertible Debentures (NCD) issue of A.K. Capital Finance Limited (AKCFL) factors in comfortable capitalization level and moderate gearing, good resource raising ability, comfortable liquidity, adequate profitability, healthy asset quality and experience of the promoter and the management. The A. K. Capital group has a track record and established presence in the debt capital markets through the parent entity A. K. Capital Services Limited (AKCSL) which is a SEBI registered Category I merchant banker having a strong institutional & retail client base.

As per its stated policy, the company would maintain overall gearing (debt / tangible net worth) of up to 3x. The company will not invest more than 20% of its business assets (referred to as 'Assets Under Management; AUM') in instruments / entities in 'BBB' category or unrated exposures and will at all points of time have at least 20% of its AUM in Government Securities G Secs / SDL / T-Bills/AAA/ AA category rated instruments / entities and liquid assets (as defined in the liquidity policy of the company). Further, the company would maintain six months of principal term debt repayment obligations in liquid assets at all times. Any material deviation from the stated policy would continue to be a key rating sensitivity.

The rating also takes note of the income volatility due to dependence on debt capital markets, moderate scale of operation and increasing competition and high borrower concentration risk due to its nature of its corporate lending and investment.

Rating Sensitivities

Positive Factors: Factors that could lead to positive rating action/ upgrade:

- *Significant increase in lending and investment portfolio, while maintaining good asset quality and capitalization levels*

Negative Factors: Factors that could lead to negative rating action/downgrade:

- *Deterioration in asset quality with Net NPA to total AUM exceeding 3% on sustained basis*
- *Deterioration in profitability with ROTA falling below 1% on sustained basis*
- *Overall gearing (debt / tangible net worth) exceeding 3x*
- *Deterioration in liquidity profile with the company not maintaining six months of principal term debt repayment obligations in liquid assets as per stated policy*
- *Deterioration in the credit profile of the assets*

Detailed description of the key rating drivers

Key Rating Strengths

Comfortable capitalization levels with moderate gearing

The company is comfortably capitalized and had a tangible net worth of Rs.611 crore (standalone) as on March 31, 2021. The company reported Capital Adequacy Ratio (CAR) of 36.70% (March 31, 2020: 49.81%) and Tier-I CAR of 36.62% (March 31, 2020: 49.71%) as on March 31, 2021 with moderate overall gearing (debt / tangible net worth) at 2.04 times (March 31, 2020: 1.49 times) as on March 31, 2021. On a consolidated basis, AKCSL's gearing stood at 2.06 times as on March 31, 2021 as against 1.46 times as on March 31, 2020, while the consolidated tangible net worth of the group stood at Rs.677 crore as on March 31, 2021.

Going forward, the company has represented that it would maintain a minimum CAR of 20% at all times and would not cross overall gearing beyond 3x.

Healthy asset quality

AKCFL has a lending portfolio which comprises of loans given to borrowers as well as investment in Non-Convertible Debentures (NCD) and other debt instruments. The company has maintained healthy asset quality with Nil NPAs over the last three years. As on March 31, 2021, around 93% of AUM was in GSec / 'A' category and above rated papers which provide

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

reasonable strong liquidity as the company has flexibility to sell-down such assets.
Further, out of the total AUM, which includes term loans, loans in form of NCD, investment in G-Sec and other highly rated papers, ~43% of the total AUM exposure as on March 31, 2021 is towards treasury book (G-sec plus highly rated papers), which has low risk. AKCFL has sound risk management practices and is benefitted from the group's experience in the debt market in assessment of credit quality of the borrowers, which has helped it maintain good asset quality over the years.
CARE expects the company to maintain its strong asset quality going forward. In any case, the company will not invest more than 20% of its AUM in 'BBB' category rated instruments / entities or unrated exposures and will at all points of time have at least 20% of its AUM in Government Securities (G Secs/SDL/T-Bills), AAA / AA category rated instruments / entities and liquid assets as per its liquidity policy.

Diversified resource profile and strong liquidity
AKCFL has diversified resource base and has borrowings in form of NCD's, term loans and CC Facility from banks and CBLO Borrowings. The company's borrowings has increased by ~48% y-o-y to Rs.1,246 crore as on March 31, 2021. Out of the total borrowings, ~53% is funded by NCD, ~37% from bank lines and ~10% from Collateralized Borrowing and Lending Obligation (CBLO) segment of the Clearing Corporation of India Limited (CCIL). AKCFL has access to Cash Credit (CC) facility from banks to the tune of Rs.450 crore as on 31.05.2021
As on March 31, 2021, the liquidity profile was comfortable with no cumulative negative mismatches up to one year. As per the company's liquidity policy, the company would at all times, maintain minimum liquidity equivalent to the next 6 months of principal term debt repayment obligations. The liquidity would be maintained in form of Government backed securities, TREPS (CBLO)/REPO lending, cash and bank balance (including lien free fixed deposits), liquid mutual funds, 'AAA' rated securities, securities of public sector entities having credit rating of 'AA' and above & commercial papers with highest credit rating, in any combination at all times.

Track record of the group in debt market and experience of promoter and management team
AKCFL is a majority owned subsidiary of AKCSL which has been providing merchant banking services and is a leading player in the corporate debt market segment through management of private placements as well as public issues. The group has a large institutional client base including provident funds, banks, financial institutions, insurance companies, mutual funds and corporates and retail client base.
The management team is headed by Mr. A.K. Mittal (Managing Director and CEO) who is a first generation entrepreneur and promoter of A. K. Group with over three decades of experience in the financial services sector. The company has a second line of management having experience in the financial services sector.

Key Rating Weaknesses
Volatility in profitability parameters
AKCFL' follows a risk management practice wherein during times of uncertainty, it reduces its loan book exposure and increases the investments proportion, which exposes it to volatility in revenue profile. The company's AUM saw increased proportion of investments while the loan portfolio contracted during the last two years. During FY20, due to uncertainty in the credit market, the company's total income declined by 18.65% to Rs.182.48 crore (standalone) and Profit After Tax (PAT) declined by 20.32% to Rs.36.63 crore due to decline in AUM. During FY21, the company's total income (standalone) was stable at Rs.182.47 crore as the company's disbursement picked-up post November 2020. The company's interest expense has significantly declined by 28.11% to Rs.74.61 crore even as the borrowings increased by 47.75% to Rs.1,246.09 crore as the average cost of borrowings declined by 78 bps to 7.14%. The operating expense has increased by 17.41% to Rs.38.16 crore as the fees and commission expenses increased by 93.34% to Rs.12.85 crore, which constitutes 33.67% of the total operating expenses. Accordingly, the company reported a 37.87% increase in PAT to Rs.50.5 crore for FY21 and its Return on Total Assets (ROTA) improved by 110 bps to 3.03%.

On consolidated basis, AKCSL derives majority of its income by subscribing debt instruments from the primary market and retailing them out to its client base, which can lead to potential income volatility due to exposure to market risk of its bond portfolio. Further, the transaction volumes would depend upon the overall buoyancy in debt capital markets which can exhibit periodic volatility and impact AKCSL's income. In FY21, AKCSL's consolidated total income was Rs.289.15 crore (FY20: Rs.314.21crore) and consolidated PAT was Rs.75.05 crore in FY21 as against Rs. 51.48 crore in FY20 due to 28.44% decline in interest expense and 23.06% decline in operating expense.

High exposure to corporate segment with relatively higher borrower concentration which may be vulnerable to high provisioning in case of slippages
The company has over the years maintained good asset quality. However, due to its nature of its exposures, the company remains vulnerable to high concentration in exposure as it focuses on large ticket size corporate lending to mainly financial services entities, a sector, which has been under considerable stress for the last three years and now with the Covid-19 pandemic.

The company's top ten borrowers in the lending segment (term loan plus loans in form of NCD) constituted ~29% of the total AUM (lending segment plus treasury book) and ~85% of the tangible net worth as on March 31, 2021. The company's ability to further scale up with impeccable asset quality remains a key rating monitorable. The company's top ten exposures in the overall book (lending book plus treasury book) constitute ~36% of the total AUM and 107.14% of the tangible net worth as on March 31, 2021.

Liquidity: Strong
The company's ALM profile as on March 31, 2021 has no negative cumulative mismatches up to one year. The company had cash and bank balance of Rs.6.68 crore, G-sec investment of Rs.148.23 crore and investment in highly rated bonds of Rs.620.95 crore as on March 31, 2021. The management has indicated to maintain around 20% of its AUM in highly rated and liquid assets at all times. The company has sanctioned undrawn lines from banks to the tune of Rs.93.46 crore as on March 31, 2021 and company is among India's few NBFCs having membership of Collateralized Borrowing and Lending Obligation (CBLO) segment of the Clearing Corporation of India Limited (CCIL) (An autonomous body regulated by Reserve Bank of India). Further, comfort is drawn from the company's policy to maintain liquidity of six months of principal term debt repayment obligations at all times.

Analytical approach:
CARE has considered the standalone financial risk profile of A.K. Capital Finance Limited along with business synergies, shared brand linkage and expected support from its parent entity A.K. Capital Services Limited.

Applicable Criteria
CARE's Policy on Default Recognition
Rating Methodology: Notching by factoring linkages in Ratings
Financial Ratios – Financial Sector
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
Criteria for Short Term Instruments
Rating Methodology - Non Banking Finance Companies (NBFCs)

About the Company
AKCFL is a 98.7% subsidiary of AKCSL, a category-I merchant banker listed on Bombay Stock Exchange, as on March 31, 2021. AKCFPL was formally known as Girdhar Vanijya Pvt. Ltd. and in September 2008, the company was acquired by AKCSL.
AKCFL is a RBI registered Systemically Important Non-Deposit taking NBFC and is primarily engaged in onward lending and investment in debt market. The company is the flagship NBFC of the group and offers customized debt solutions to eligible borrowers having good repute and proven track record in the industry. The company lends to corporate entities by way of loans and advances as well as investment in credit instruments which allows the company the flexibility to down sell the instruments in a short span of time.
AKCFL has a 100% subsidiary 'Family Home Finance Private Limited' (FHFPL) which is a housing finance company registered with NHB. The company was incorporated on June 29, 2017 and had negligible loan portfolio as on March 31, 2021. The management does not intend to grow the housing finance business and would explore suitable options to monetize the HFC business.
AKCSL has been providing merchant banking services for over twenty years and is a leading player in the corporate debt market segment through management of private placements as well as public issues.

Brief Financials (Rs. crore)	FY20 (A)	FY21 (A)
Total income	182.48	182.47
PAT	36.63	50.50
Interest coverage (times)	1.45	1.88
Total Assets^	1439.04	1897.15
Net NPA (%)	Nil	Nil
ROTA (%)	1.93	3.03

A: Audited; ^: Net of intangible assets, revaluation reserve & Deferred Tax Assets (DTA)
Note: The calculations are as per CARE Ratings' calculation
Status of non-cooperation with previous CRA: Not Applicable
Any other information: Not Applicable
Rating History for last three years: Please refer Annexure-2
Complexity level of various instruments rated for this company: Annexure 3

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Debentures-Non-Convertible Debentures	Proposed	-	-	-	100	CARE AA-; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Fund-based - LT-Working Capital Demand loan	LT	-	-	-	-	-	1)Withdrawn (29-Mar-19)
2.	Commercial Paper	ST	-	-	-	-	1)Withdrawn (26-Sep-19)	1)CARE A1+ (29-Mar-19)
3.	Fund-based - LT-Term Loan	LT	-	-	-	-	-	1)Withdrawn (29-Mar-19)
4.	Commercial Paper-Commercial Paper (Standalone)	ST	20.00	CARE A1+	1)CARE A1+ (16-Jun-21)	-	-	-

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
5.	Debentures – Non-Convertible Debentures	LT	100.00	CARE AA-; Stable	-	-	-	-

Annexure 3: Complexity level of various instruments rated for this company

Sr No	Name of instrument	Complexity level
1	Commercial Paper-Commercial Paper (Standalone)	Simple
2	Non-Convertible Debentures	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Contact us

Media Contact
Mradul Mishra
Contact no.: +91-22-6837 4424
Email ID: mradul.mishra@careratings.com

Analyst Contact 1
Mr. Aditya Acharekar
Contact no.: 022-6754 3528
Email ID: aditya.acharekar@careratings.com

Analyst Contact 2
Mr. Sanjay Kumar Agarwal
Contact no.: (022) 6754 3500 / 582
Email ID: sanjay.agarwal@careratings.com

Business Development Contact
Mr. Ankur Sachdeva
Contact no.: 91 98196 98985
Email ID: ankur.sachdeva@careratings.com

About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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